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Supreme Court of the United States

OCTOBER TERM, 1923

No. 238

The

LIBERTY NATIONAL BANK OF ROANOKE, VIRGINIA, A CORPORATION,

PETITIONER

vs.

JAMES A. BEAR, TRUSTEE IN BANKRUPTCY, of W. L. BECKER & COMPANY, and ROANOKE PROVISION COMPANY, and W. L. BECKER, SR., and W. L. BECKER, JR., INDIVIDUALLY,

RESPONDENT

PETITIONER'S REPLY BRIEF

To the Honorable the Chief Justice and Associate Justices of The Supreme Court of the United States

In this brief the Petitioner is referred to as the Bank and Respondent as Trustee.

STATEMENT OF THE CASE

In the main, the Trustee's brief correctly states the facts, but we object to the following recitals as misleading:

On page 2, in the 2nd paragraph from the bottom, it is said that the joint answer of the partners was "signed

by them in their individual capacities." This is not borne out by the record or facts. The individual petition of August 6th, 1920, was against the two partnerships alone, and they only were adjudicated bankrupts in that proceeding. The Court expressly refused in the petition against the partnerships to adjudicate the individual partners. See, Record, page 51, where Judge McDowell says:

> "The order of adjudication of Aug. 20th, 1920, declares the partnership to be a bankrupt and distinctly fails to declare the individuals composing the partnership to be bankrupts."

So, however signed, the answer was the answer of the partnerships.

ARGUMENT

We will reply to several points in the Trustee's brief in the same order that they appear:

I.

On page nine, the Trustee says:

> "The partnership and its members were in fact insolvent."

This is the first time the Trustee has said anything about insolvency. He is attacking a judgment and seeking to avoid it, and he must both allege and prove insolvency. The Trustee's objections on page 21 of the Record make no averment of insolvency of either the firm or the individuals.

Black on Bankruptcy 3rd Ed. Sec. 595, page 1229, says:

> "The trustee in bankruptcy, assailing a judgment or transfer as preferential, must assume the burden of showing the insolvency of the debtor by satisfactory and sufficient evidence."

Collier, 8th Ed. page 650, says:

> Insolvency "is a question of fact, and the burden of showing it is on him who alleges it * * * it must be alleged and found as a fact."

The individual partners must have been proven to have been insolvent **at the time the Bank's judgment was recovered** to render it a voidable preference. Black On Bankruptcy, 3rd Ed. page 1250, says:

> "One thing absolutely essential to constitute a voidable preference is that the debtor should have been insolvent at the time it was given, and the trustee has the burden of proving this fact. The mere fact that the debtor was afterwards adjudged bankrupt raises no presumption that he was insolvent at any given time within four months prior to the filing of the petition. And the giving of a confession of judgment does not of itself raise a presumption of insolvency."

No where has the trustee made any allegation that the individual partners were insolvent when the Bank's judgment was recovered, and this omission is fatal.

The quotations taken by the Trustee from the Bank's petitions for appeal and review, appearing on page 10 of his brief, were made many months after the recovery of the Bank's judgment, and in no proper sense can they be held to apply to conditions at the date of the recovery of the judgment. They are, therefore, not relavant or pertinent.

At the bottom of page 10, counsel for the Trustee has fallen into a grievous error in attempting to shift the burden by asserting that the objection of insolvency "comes too late and cannot now be heard." Black on Bankruptcy, Sec. 614, says:

> "In an action to set aside or recover a transfer, incumbrance or payment, alleged to constitute an unlawful preference, the burden of proof is on the trustee in bankruptcy to establish the existance of

each of the statutory elements of a voidable preference."

We have shown, as we think, that the Trustee has not borne his burden.

On page 11 of Trustee's brief it is asserted, under bold type, "that the adjudication of the partnership was in effect an adjudication of the individual members."

> This statement is in direct conflict with the Court's order adjudicating the partnerships and refusing to adjudicate, at the same time, the individual members of the firm (Record, page 51). The Trustee by argument seeks to attain what the Court declined by its order, and attempts to accomplish by indirection, what the Court refused directly. Such a position seems all the more strange, when we remember that all the powers the trustee for the partnerships has are derived from the selfsame order.

At the top of page 12, Trustee quotes a part of General Order No. 8 in support of his argument, that the adjudication of the partnerships was in effect an ajudication of the individual members. The point is not well taken. This order was copied from one drawn under the Acts of 1867, where the partnership was not an entity, and where the only way to put a partnership into bankruptcy was to adjudicate the individuals. The law is entirely different under the Act of 1898. We quote from In re Samuels and Lesser 30th A. B. R. page 297:

> "It is said that General Order No. 8 controls, but that is by no means clear. The order was copied from one drawn under the Act of 1867, which did not recognize the firm entity, and it does not assume the possibility of a firm adjudication without adjudication against the partners separately."

In the middle paragraph, same page, it is said:

> "And from this moment, with their consent, their estates were under the jurisdiction of the bankruptcy court for distribution of their property among the several classes of creditors."

We do not think the record shows that there is any proper foundation for this utterance. The written offer of compositions made by the partnerships distinctly says that **"the rights of the individual creditors are not herein sought to be, and will not be, affected by this composition if confirmed," and that no discharge of individual debts was sought** (Record page 24, Sec. 8).

Again, in the Bank's proof of debt (Record page 19) it is averred:

> "That while a receiver was appointed by the Judge of this court for the partnerships on August 7th, 1920, said receiver had no authority or control over any of the individual assets and property of the individuals of the partnerships, and at no time took control, or attempted to take control, of any of the individual assets and property, but all of said individual assets and property remained in the possession and exclusive control of the individuals, to-wit, W. L. Becker, Sr., and W. L. Becker, Jr., and said individuals asserted their exclusive possession and control of said individual property by using and enjoying the two residences, which are part of the individual assets, with their families, and by giving a deed of trust on their individual real estate, without the consent or order from any court to do so, with which to secure money to offer as a composition to their creditors."

This averment is no where denied by the Trustee, and, therefore, is an admitted fact.

It is, therefore, respectfully submitted that the Trustee erred when he made the statement above quoted, and as a matter of fact, the individual assets were not before the court for distribution from the filing of the lists.

The Trustee cites the case of DICKAS v. BARNES 140 Fed. 849; 15 A. B. R. 566. This case when properly considered, in the light of the facts of the instant case ~~now considered, in the light of the facts of the instant case~~, is an authority for the Bank. The syllabus says:

> "Upon the adjudication of an unincorporated company in a jurisdiction where it is held to be a partnership the court of bankruptcy may take possession of and administer the property of one of the members whom it could not adjudge bankrupt, **so far as necessary in the settlement of the partnership assets."**

In the Bank's brief attached to the petition, on page 14, FRANCIS v. McNEAL 26 A. B. R. 560, is quoted where the court says: that "it may well be doubted."

> "Whether, where the act of bankruptcy charged against a partnership is one that does not involve insolvency, an adjudication against the partnership only draws into the proceeding the individual assets of the unadjudicated member."

FRANCIS v. McNEAL was decided later than the Dickas case, and was affirmed by this Honorable Court, and, therefore, is the controlling decision. We feel fully warranted, therefore, in asserting that the Dickas case, Meyer case and Stokes case, cited on pages 12 and 13 of Trustee's brief, are not authorities in point.

However, let us consider briefly the Dickas case. Particular attention is directed to the language underscored above, "so far as necessary in the settlement of the partnership assets." For the sake of argument, we might admit that where a partnership alone is adjudicated, that the court could reach out after the individual assets, if there was a surplus above individual debts, but even if this be granted, the true principal would limit the administration to the language above, "so far as necessary in the settlement

of the partnership assets." How could the court properly go further, and what reason would there be for it to undertake to go further?

We quote In re SAMUELS & LESSER, 30 A. B. R. page 296, where the court says:

> "It seems to me obvious justice that his whole separate estate ought not to be drawn into the bankruptcy court for administration unless that be true and so far, indeed, Judge LANNING felt bound to go in FRANCIS v. McNEAL, supra, to avoid unjust results. But though the worst aspect of the doctrine would be relieved by its limitation to cases where the partner was individually insolvent, it is none the less always ~~obvious~~ obnoxious in principle, since the partner's estate ought not to be drawn into bankruptcy at all unless he has committed an act of bankruptcy. It is true that he avoids the stigma of the name, but there may be more concerned than that to his creditors. For instance, does the administration of the separate estate presuppose that the firm acts of bankruptcy invalidate execution liens of the individual creditors? If not, the bankruptcy court will administer the separate estate without regard to sections 67c or 67f. If, on the other hand, the firm acts of bankruptcy do affect the status of the individual creditors, it is a clear anomaly under the law."

In the instant case it is admitted, and no where denied: that **there will be no surplus from the individual assets to go to the partnership creditors**; that the individual partners had committeed no act of bankruptcy; that they were not parties defendant to the petition against the partnerships; that the court refused to adjudicate the individuals along with the partnerships; that the trustee of the partnerships was elected by the partnership creditors alone, and that after the Bank's judgment was more than four months old the individuals were adjudicated on their voluntary petition and a trustee was elected by the individual creditors to administer the individual assets.

Under these facts, how could the trustee for the partnerships legally or with propriety assert any claim against the individual assets, or the right to administer the same? Any effort on his part to do so would be unwarranted, and he would be exceeding his authority.

The trustee devotes more than three pages of his brief beginning on page 14, to a discussion of the case of FRANCIS v. McNEAL, 228 U. S. 695, 57, L. Ed., page 1029; 30 A. B. R. 247, also reported 26 A. B. R. 558. We have discussed this case in the brief accompaning the petition, on pages 16 and 17, and deem is unnecessary to make further reference thereto.

On page 17 of brief, the Trustee again discusses the question of insolvency, becoming confused, and reaching a false conclusion in saying "that the adjudication of the firm as bankrupt is bound in the nature of things to be an adjudication of the individuals partners as insolvent."

It is true that a partnership cannot be insolvent unless the individual partners are insolvent, and it is likewise true, that where the alleged act of bankruptcy involves insolvency, that the partnership cannot be adjudicated unless the individuals are parties to the petition, and they, as well as the partnership, are shown to be insolvent, but it is absolutely incorrect to say that in the instant case adjudication of the partnership was an adjudication of the individual partners to be insolvent. The act of bankruptcy committeed by the partnerships was the first part of the fourth act of bankruptcy, to-wit, having "made a general assignment for the benefit of his creditors." The partnerships having made a general assignment, the act of bankruptcy was complete, whether they were solvent or insolvent, and the District Judge was not called upon to inquire into the solvency or insolvency of the partnerships or the members thereof. The insolvency was non-essential to the adjudication of the partnerships.

It is manifest, therefore, that counsel for the trustee, and the learned Judges of the Circuit Court are in error in concluding that the adjudicating of the partnerships meant an adjudication of the individuals also.

But where the act of bankruptcy committed by the partnership does not involve insolvency, the partnership may be adjudged a bankrupt without adjudging the individuals. Such is the instant case. To hold that in every case where a partnership makes a general assignment, and thereby commits an act of bankruptcy, the partnership cannot be adjudicated without ipso facto adjudicating the individuals will completely wipe out the entity doctrine in such cases, and will be a great injustice to individuals composing partnerships. To so hold would be a distinct step backward, for while under the bankruptcy act of 1867, a partnership was adjudicated by adjudicating the individuals, such is not true under the act of 1898. Collier 13th Ed. Vol. 1, page 233, says:

> "A partnership now is something other than under the law of 1867. There the words, were, 'two or more persons who are partners in trade.' Now it is a 'partnership' that 'may be adjudged a bankrupt.' This phrasing coupled with other clauses, has led to the doctrine that a partnership is in bankruptcy a legal entity—a joint relation where the idenity of the members has been lost—and that, therefore, the individuals and the partnerships are entities separate and distince from each other'."

> "Application Of Doctrine—A partnership being a distinct entity, it owns its property and owes its debts apart from the individual property of its members which it does not own, and apart from the individual debts of its members which it does not owe. Under this principle a partnership as an entity may be adjudged to be a bankrupt, irrespective of any adjudication against the individual members."

II.

We refrain from discussing the Trustee's Division No. 2, on page 19 of his brief, as this has been answered, as we believe, in the discussion of other points.

III.

Under Division No. 3, under the head of "Litigation Pending" the Trustee rehearses much that has been stated in previous parts of his brief, and rather invokes the affirmance of the decision of the Circuit Court because of the unfortunate plight of the partnership creditors. This line of argument is in the nature of a request to ignore well established legal rules and principles, and wipe out the Bank's judgment without proper and sufficient allegation being made, and proof introduced by the Trustee. Later in this brief will be set out the essential allegations for the avoidance of a judgment, with none of which the Trustee has complied.

The Trustee for the partnership creditors has no ground to complain if the Bank collects its judgment from the individual assets, because it is admitted that there will be no surplus from the individual assets. Furthermore, partnership creditors and individual creditors are not in the same class and the Bank would be getting no preference over a creditor of the same class. If the Bank collects every dollar of its debt it doesn't take a penny from the partnership creditors. What ground have they or their trustee, therefore, to complain?

The trustee for the individual creditors cannot complain, because, when the individuals were adjudicated the Bank's debt was more than four months old. So the plea for equity comes with poor grace from the Trustee for the partnerships or the Trustee for the individuals.

Again, on page 24, Paragraph 1, Trustee says that "the bankruptcy act is dual in its operation. On the one hand

it operates in rem * * * * . On the other hand in personam granting persons adjudged bankrupts a discharge from their debt," etc.

This line of argument, while somewhat plausible, is not logical. It recoils upon the Trustee. He seems to argue that this court should by indirection destroy the Bank's judgment by taking away the assets to which it has attached through the Bank's diligence, while the Court would be powerless to grant the judgment debtors a discharge. The Bank's judgment cannot be annulled and avoided unless the individuals have been adjudged bankrupts within four months, and if the judgment can't be avoided except in this manner, the assets out of which it could be collected cannot be taken away from it. So, the Trustee has asked the court in the partnership proceedings to take away the individual assets from the lien of the Bank's judgment, when he is forced to admit that in that proceeding a discharge could not be granted to the individuals.

Where an individual is in bankruptcy and makes proper application according to law he can get his discharge, but no one would be so bold as to contend that in the partnership proceedings in this case the individuals could have gotten a discharge, for it is admitted that they were not before the court at that time. Hence, it follows that this line of argument from the standpoint of the Trustee becomes absurd, but from the viewpoint of the Bank it becomes a very potent reason why the bankruptcy of the partnerships in no sense annulled or avoided the Bank's judgment against the individuals.

IV.

Under Division 4, page 24, of Trustee's brief it is said that "the assignment of error should be overruled," and that Sections 67c and 67f are to be construed in connection with the other provisions of the bankruptcy act. This is true, but in so doing the court will not ignore and completely wipe

out said sections, which it would have to do if it followed and adopted the Trustee's argument.

CONCLUSION

Throughout this case the Trustee for the partnerships and the trustee for the individuals has failed to conform to the essential requirements, both in allegation and proof, which all of the authorities hold are necessary to avoid a judgment. Black On Bankruptcy, 3rd Ed. page 1246 says:

> "The four essential allegations of the complaint are (1) that the bankrupt was insolvent when the alleged preference was given; (2) that it was within four months prior to the bankruptcy; (3) that the effect of the enforcement of the judgment or transfer will be to enable the defendant to obtain a greater percentage of his debt than any other creditor of the same class; (4) that the defendant had reasonable ground to believe that a preference would result from the transaction. The omission of any one of these allegations will render the complaint demurrable."

A comparison of the above four necessary and required allegations, in any proceeding seeking to avoid a judgment, with the objections of the Trustee as found on pages 21 and 22 of the record, will disclose the fact that he has failed to aver any one of the four. The Bank's motion to dismiss the Trustee's appeal, and its demurrer thereto, (Record, pages 56, 57 and 58) should therefore, have been sustained by the learned Judges of the Circuit Court of Appeals, and their failure so to do, seems clearly to be error, for which this court will reverse said decision.

The Bank recovered three judgments; one against the Roanoke Provision Company (A partnership composed of W. L. Becker, Sr., and Jr.,); another against W. L. Becker, Sr., individually; and a third against W. L. Becker, Jr., individually on a negotiable note made jointly by W. L. Becker, Sr., and the Roanoke Provision Company, and endorsed by

W. L. Becker, Sr., and W. L. Becker, Jr. The individuals were sued individually, as well as in their partnership capacity. Process was served on them in their individual capacity, and judgment rendered and docketed in the same manner (Record page 22, Sec. 1, Summary Evidence).

These separate judgments against the individuals could have been avoided by the filing of a petition in bankruptcy by or against the individuals within four months. No petition in bankruptcy was filed within the four months, and it is clear, therefore, that the learned Judge of the District Court was correct in holding that the judgments against the individuals had not been avoided. The court says:

> "The wording of the order of adjudication was not an inadvertance, but was the result of the construction I have put on the Bankrupt Act since my first connection with it. The refusal to adjudge the individuals composing the firm to be bankrupt was, if erroneous, an error which had to be appealed from within ten days from August 20th, 1920 (Sec. 25 B. A.). As no appeal was taken within the time allowed by law, neither this court nor any other court can now correct the supposed error. The result is that the individuals composing the partnership have, in the partnership proceedings, never been adjudged. Both the filing of a petition within fouth months, and an adjudication thereon are necessary to nullify a lien of a judgment."

It is therefore respectfully submitted, that the decision of the Circuit Court of Appeals is erroneous and should be reversed.

JAS. D. JOHNSTON,
Counsel for Petitioner.